

REPORT OF EXAMINATION
OF THE
FINANCIAL PACIFIC INSURANCE COMPANY

AS OF
DECEMBER 31, 2003

Participating State
and Zone:

California

Filed April 12, 2005

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San Francisco, California
March 11, 2005

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition Subcommittee
Commissioner of Insurance
Virginia Bureau of Insurance
Richmond, Virginia

Honorable John Morrison
Secretary, Zone IV-Western
Commissioner of Insurance and Securities
Montana Department of Insurance
Helena, Montana

Honorable John Garamendi
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman and Commissioners:

Pursuant to your instructions, an examination was made of the

FINANCIAL PACIFIC INSURANCE COMPANY

(hereinafter referred to as the Company) at its home office located at 3850 Atherton Road, Rocklin, California 95765.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 1998. This examination covers the period from January 1, 1999 through December 31, 2003. The examination was made pursuant to the National Association of Insurance Commissioners' plan of examination. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions, an evaluation

of assets, and a determination of liabilities as of December 31, 2003, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; business in force by states; and sales and advertising.

COMPANY HISTORY

On December 4, 2002 the parent company, Financial Pacific Insurance Group, Inc. (Group) participated in a placement of \$5 million of floating rate capital securities (Trust Preferred Securities) issued by Financial Pacific Statutory Trust I (Trust), a statutory trust created under the laws of the State of Connecticut. The Trust Preferred Securities mature in December 2032, and require quarterly distributions of interest by the Trust to the holders of the Trust Preferred Securities at 3 month London Interbank Offered Rate (LIBOR) rate plus 400 basis points.

The Trust used the proceeds from the sale of the Trust Preferred Securities combined with the proceeds from the sale by the Trust to the Group of its common stock (\$155,000) to purchase \$5,155,000 of a Floating Rate Junior Subordinated Deferrable Interest Debenture due 2032 in the principal amount of \$5,155,000 issued by the Group. The net proceeds to the Group from the sale of the Debenture to the Trust were used by the Group to payoff its remaining \$1.5 million in investor debt as well as the term loan with U.S. Bank. The Group subsequently purchased a five year interest rate swap to fix the interest rate at 7.5%.

During 2003, the Group participated in two additional placements of trust preferred securities. On May 15, 2003 the Group participated in a placement of \$3 million of fixed/floating rate capital securities (Trust Preferred Securities) issued by Financial Pacific Statutory Trust II (Trust II), a statutory trust created under the laws of the Connecticut Statutory Trust Act. The Trust Preferred Securities mature in May 2033, and require quarterly distributions of interest by the Trust II to the holders of the Trust Preferred Securities at a fixed interest rate of 7.35% until May

15, 2008, at which time it converts to a floating rate of 3 month LIBOR rate plus 410 basis points.

The Trust II used the proceeds from the sale of the Trust Preferred Securities combined with the proceeds from the sale by the Trust II to the Group of its common securities (\$93,000) to purchase \$3,093,000 of a Fixed/Floating Rate Junior Subordinated Deferrable Interest Debenture due 2033 in the principal amount of \$3,093,000 issued by the Group. The net proceeds to the Group from the sale of the Debenture to the Trust II were used by the Group to payoff its \$2.0 million line of credit with U.S. Bank with the remaining \$.9 million, net of origination fees, transferred to the Company as a capital infusion.

On September 30, 2003 the Group participated in a placement of \$7.5 million of floating rate capital securities (Trust Preferred Securities) issued by Financial Pacific Trust 3 (Trust 3), a Delaware statutory trust. The Trust Preferred Securities mature in September 2033, and require quarterly distributions of interest by the Trust 3 to the holders of the Trust Preferred Securities at a floating rate of 3 month LIBOR rate plus 405 basis points.

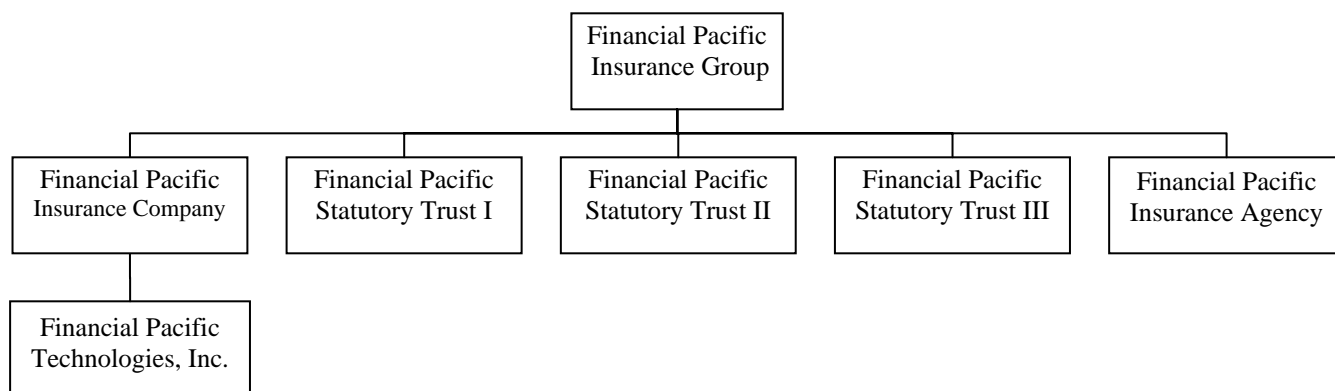
The Trust 3 used the proceeds from the sale of the Trust Preferred Securities combined with the proceeds from the sale by the Trust 3 to the Group of its common securities (\$240,000) to purchase \$7,740,000 of Floating Rate Junior Subordinated Deferrable Interest Debenture due 2033 in the principal amount of \$7,740,000 issued by the Group. The net proceeds to the Group from the sale of the Debenture to the Trust were used by the Group to transfer \$7.3 million, net of origination fees, to the Company as a capital infusion.

In addition to the cash contributions made by the Group in 2003, the following are cash contribution made to the Company from 1999 through 2002: \$1 million in 1999; \$725,000 in 2000; and \$2,484,000 in 2002.

The Group is dependent on dividends from the Company to service its debts. From 1999 to 2003, the Company declared and paid cash dividends to the Group in the amount of \$1,725,000, \$935,000, \$770,000, \$1,028,000, and \$70,000.

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system of which Financial Pacific Insurance Group, Inc., (Group), a Delaware corporation, is the ultimate controlling entity. The Group is primarily owned by three investor groups: Firemark Global Insurance Fund, L.P., FinPac Partners (J. Christopher Lewis and Patrick C. Haden, the general partners) and St. Paul Fire & Marine Insurance Company. All outstanding shares of the Company are owned by the Group. The following abridged organizational chart depicts the Company's relationship within the holding company system as of December 31, 2003 (all ownership is 100%):



Management of the Company is vested in a four-member board of directors. Following are lists of directors and the principal officers of the Company as of December 31, 2003:

Directors

Name and Residence

Stephen E. Adamson
Los Angeles, California

John R. Hollingshead
Roseville, California

Principal Business Affiliation

Principal of Celerity Partners

Vice President, Corporate Counsel and
Secretary
Financial Pacific Insurance Company

Directors (continued)

Name and Residence

Principal Business Affiliation

Robert T. Kingsley
Davis, California

President and Chief Executive Officer
Financial Pacific Insurance Company

Artur A. Turner
Folsom, California

Vice President, Treasurer and Chief
Financial Officer
Financial Pacific Insurance Company

Principal Officers

Name

Title

Robert T. Kingsley
John R. Hollingshead

President and Chief Executive Officer
Vice President Corporate Counsel and
Secretary

Artur A. Turner

Vice President, Treasurer and Chief
Financial Officer

Intercompany Agreements

The Company entered into an intercompany agreement with its affiliates effective January 1, 1998. The agreement provides that the affiliated companies periodically share with each other certain financial and administrative services. The agreement also provides that each subsidiary will calculate its federal income tax liability on a separate return basis. Settlement among the affiliates is based on the actual cost incurred. The Company also maintains employment agreements with its officers.

As of December 31, 2003, the Company had not filed the agreement and its addendum for approval with the California Department of Insurance (CDI). The Company has subsequently submitted to the CDI a filing pursuant to California Insurance Code (CIC) Section 1215.5(b) (4), on December 23, 2004.

Insurance Holding Company System Regulatory Act

During the period covered by this examination, the Company made certain cash transfers to its parent, which were not reported to the CDI as required by CIC Section 1215.4. It is recommended that the Company report these transactions to the CDI pursuant to CIC Section 1215.4.

During the period covered by this examination, the Company incurred certain expenses for the benefit of its parent, Group, which were not reimbursed by the Group. The Company has stated that during 2004, the Group began to reimburse the Company for expenses incurred on the Group's behalf.

CORPORATE RECORDS

The Company had on file conflict of interest statements for its directors, officers, and key employees for the year 2000 only, but had not required annual reporting of its conflict of interest statements in the subsequent years. In lieu of annual conflict of interest statements, the Company required that its directors and officers annually sign "Acknowledgment of Receipt of Human Resources Policy Manual." The Manual requires all employees to fully disclose any potential conflict of interest. It is recommended that the Company establish written procedures to require annual conflict of interest reporting for its directors, officers and key employees.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2003, the Company was licensed as a multi-line property and casualty insurer in the following 19 states: Alaska, Arizona, Arkansas, California, Colorado, Idaho, Kansas, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oklahoma, Oregon, South Dakota, Utah, Washington, and Wisconsin. In 2003, \$79.3 million or 86% of its direct premium was written in California.

The Company writes the majority of its business in rural markets in Northern California with moderate geographical diversification into Oregon, Nevada and Arizona. The business written outside of these four states is limited to the mail order distribution of license and permit surety bonds.

The Company writes commercial package policies and surety business. The Company's commercial package business consisted of commercial multiple peril (including property, inland marine, fidelity and general liability coverages), auto liability, auto physical damage, equipment breakdown and pollution policies. The majority of the Company's business was written for small to medium size businesses. The commercial multiple peril business comprised 72% of the Company's 2003 direct premium written. The Company targets four main segments of commercial multiple peril business: artisan contractors, commercial property owners, light industrial risks and specialty programs. The Company writes business through approximately 230 independent agents.

GROWTH OF COMPANY

During the examination period, the Company experienced substantial premium growth. Direct premiums written have grown from \$43.2 million in 1998 to \$92.7 million in 2003. The significant growth in direct premiums written during the examination period is primarily attributed to price increases as the number of in-force policies, excluding the barber program and surety, increased by only 6% (from 7,613 in 1998 to 8,033 in 2003). The Company also expanded geographically, primarily in Nevada and Oregon, as premiums written outside of California grew from \$0.2 million in 1998 to \$13.4 million in 2003.

REINSURANCE

Assumed

The Company did not assume any reinsurance during the examination period.

Ceded

<u>Type of Contract</u>	<u>Reinsurer</u>	<u>Company's Retention</u>	<u>Reinsurer's Maximum Limit</u>
<i>Casualty Excess of Loss</i>	ALEA North America Insurance Company – 10%; Continental Casualty Company – 47.5%; Folksamerica Reinsurance Company – 5%; Partner Reinsurance Company of the US – 25%; QBE Reinsurance Corporation – 12.5%.	First layer – \$250,000 ultimate net loss each insured, each occurrence Second layer - \$500,000 ultimate net loss each insured, each occurrence	First layer – \$250,000 excess of \$250,000 ultimate net loss each insured, each occurrence Second layer – \$500,000 excess of \$500,000 ultimate net loss each insured, each occurrence
<i>Automobile Casualty Excess of Loss</i>	Continental Casualty Company – 20%; Folksamerica Reinsurance Company – 15%; Harco National Insurance Company – 10%; Partner Reinsurance Company of the US – 15%; QBE Reinsurance Corporation – 10%; Swiss Reinsurance America Corporation – 30%.	First layer – \$100,000 ultimate net loss each insured, each occurrence Second layer – \$500,000 ultimate net loss each insured, each occurrence	First layer – \$400,000 excess of \$100,000 ultimate net loss each insured, each occurrence Second layer – \$500,000 excess of \$500,000 ultimate net loss each insured, each occurrence
<i>Commercial Excess Liability</i>	American Reinsurance Company	\$1 million each occurrence	100% of \$10 million in excess of \$1 million each occurrence
<i>Property Quota Share</i>	Continental Casualty Company – 27.5%; Harco National Insurance Company – 15%; Partner Reinsurance Company of the US – 20%; QBE Reinsurance Corporation – 20%; Swiss Reinsurance America – 17.5%.	20% of the net liability	80% of the net liability up to \$2 million.

<u>Type of Contract</u>	<u>Reinsurer</u>	<u>Company's Retention</u>	<u>Reinsurer's Maximum Limit</u>
<i>Commercial Property Excess of Loss</i>	General Reinsurance Corporation	Commercial property - \$2 million each risk Apartments - \$1.5 million each risk	Commercial property - \$8 million each risk excess of \$2 million each risk Apartments - \$6 million excess of \$1.5 million each risk
<i>Contingent Excess of Loss</i>	Montpelier Reinsurance Ltd. – 14%; Lloyd's Underwriters – 86%.	Casualty - \$2.0 million ultimate net loss each insured, each occurrence Property - \$2.0 million ultimate net loss per risk, per occurrence Fidelity - \$1.0 million ultimate net loss per risk, per occurrence Surety - \$3.5 million ultimate net loss any one bond or any one principal.	Casualty - \$4 million excess of \$2 million each insured, each occurrence Property - \$4 million excess of \$2 million ultimate net loss per risk, per occurrence Fidelity - \$4 million excess of \$1 million per risk, per occurrence Surety - \$4 million excess of \$3.5 million any one bond or any one principal
<i>Casualty Quota Share</i>	Berkley Insurance Company	60% of ultimate net loss of \$100,000 each insured, each occurrence	40% of ultimate net loss of \$100,000 each insured, each occurrence
<i>Surety Excess of Loss</i>	General Reinsurance Corporation	\$200,000 each principal plus: First Excess Cover – 10% of \$1.8 million excess of \$200,000 Second Excess Cover – 7.5% of \$1.5 million excess of \$2 million	First Excess Cover – 90% of \$1.8 million excess of \$200,000 each principal Second Excess Cover – 92.5% of \$1.5 million excess of \$2 million each principal
<i>Environmental Liability Quota Share</i>	Greenwich Insurance Company	None	100% of \$2 million
<i>Equipment Breakdown Quota Share</i>	The Hartford Steam Boiler Inspection and Insurance Company	None	100% of \$25 million any one accident

The business ceded under the environmental liability and equipment breakdown reinsurance contracts are coverages issued under commercial multiple peril, and are written not on a standalone basis.

Insolvency Clauses:

The insolvency clauses in some reinsurance agreements are not in compliance with California Insurance Code (CIC) Section 922.2(a) (2).

The insolvency clause in the commercial excess liability agreement gives the reinsurer the right to offset in the event of the insolvency of the ceding company; this is not permitted under CIC Section 922.2(a) (2).

The insolvency clause in the environmental liability quota share agreement contains references to New York insurance laws.

It is recommended that the reinsurance agreements be amended to comply with CIC Section 922.2(a) (2), and any reference to New York laws be deleted.

Offset Clauses:

The offset clauses in the commercial excess liability and the casualty quota share agreements were unacceptable because it mentions “insolvency.” By including “insolvency” in an offset clause, it places the offset clause in the context of an insolvency setting and negates the provisions of the insolvency clause (which requires the reinsurer to pay its portion of the loss without diminishment). Furthermore, the offset clause in the commercial excess liability agreement allows either party to withhold premiums or loss payments as collateral at any time from the other party when the other party is in default or subject to liquidation, rehabilitation, reorganization or conservation proceeding. The offset provisions in the above reinsurance contracts are in violation of CIC Section 922.2(a) (2).

It is recommended that the offset clauses in the reinsurance agreements be amended to remove any reference to “insolvency.”

Termination Provisions:

The termination provisions in the casualty excess of loss, automobile casualty excess of loss and property quota-share agreements allow either party to terminate the agreement if the other party's surplus is reduced by 25%, the other party has been ordered to cease writing business, or the other party has become insolvent. Per SSAP No. 62, paragraph 7, an entry of an order of rehabilitation or liquidation cannot constitute an anticipatory breach by the reporting entity nor be grounds for retroactive revocation or retroactive cancellation of any contracts of the reporting entity. It is recommended that the reinsurance agreements be amended to comply with SSAP No. 62, paragraph 7, of the NAIC Accounting Practices and Procedures Manual.

Governing Law Clauses:

The governing law clause in the environmental liability quota-share agreement requires the agreement to be governed by and interpreted in accordance with the laws of the State of New York. It is recommended that this clause be deleted.

Reinsurance Commutation

Effective March 31, 2003, the Company commuted all reinsurance agreements with Gerling Global Reinsurance – US Branch and Gerling Global Reinsurance of America (collectively Gerling). These reinsurance agreements include the property quota-share, property excess of loss, casualty excess of loss, and facultative agreements with Gerling. As a result of the commutations, the Company received cash of \$6.4 million, reinsurance recoverables were reduced by \$2.5 million, and a gain on commutation of \$3.9 million was recorded. The gain on commutation was then offset by a corresponding increase in reserves to reflect a more conservative valuation of the exposure that had been previously ceded to Gerling.

ACCOUNTS AND RECORDS

Information Systems Control Environment

A limited review was made of the Company's general controls over its information systems. As a result of the review, weaknesses were noted in areas such as business continuity, physical security, information security, and operational controls. The weaknesses noted were presented to the Company along with recommendations to strengthen its controls.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2003

Underwriting and Investment Exhibit for the Year Ended December 31, 2003

Reconciliation of Surplus as Regards Policyholders from December 31, 1998 through December 31, 2003

Statement of Financial Condition
as of December 31, 2003

	<u>Ledger and Non-ledger Assets</u>	<u>Non- Admitted Assets</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
<u>Assets</u>				
Bonds	\$116,062,739	\$	\$116,062,739	
Real estate:				
Property occupied by the company	350,380		350,380	
Cash and short-term investments	7,051,518		7,051,518	
Investment income due and accrued	1,313,437		1,313,437	
Premiums and considerations:				
Uncollected Premiums and agents' balances in course collection	2,290,948	79,435	2,211,513	(1)
Deferred premiums, agents' balance and installments booked but deferred and not yet due	19,599,249		19,599,249	(1)
Reinsurance:				
Amounts recoverable from reinsurers	898,640		898,640	
Net deferred tax asset	3,907,523	1,420,528	2,486,995	
Guaranty funds receivable or on deposit	8,606		8,606	
Electronic data processing equipment	105,222		105,222	
Furniture and equipment	665,257	665,257	-	
Receivable from parent, subsidiaries, and affiliates	<u>365,126</u>	<u> </u>	<u>365,126</u>	
Total assets	<u>\$152,618,645</u>	<u>\$2,165,220</u>	<u>\$150,453,425</u>	
<u>Liabilities, Surplus and Other Funds</u>				
Losses			\$ 46,124,719	(2)
Loss adjustment expenses			18,341,859	(2)
Commissions payable, contingent commissions and other similar charges			1,923,989	
Other expenses			3,480,577	
Taxes, licenses, and fees			491,488	(3)
Federal and foreign income taxes			12,586	
Unearned premiums			16,549,097	
Ceded reinsurance premiums payable			<u>22,954,066</u>	
Total liabilities			109,878,381	
Common capital stock		\$ 3,003,000		
Gross paid-in and contributed capital		24,418,974		
Unassigned funds		<u>13,153,070</u>		
Surplus as regards policyholders			<u>40,575,044</u>	
Total liabilities, surplus and other funds			<u>\$150,453,425</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2003

Statement of Income

Underwriting Income

Premiums earned		\$32,586,206
Deductions:		
Losses incurred	\$18,834,449	
Loss expenses incurred	6,843,974	
Other underwriting expenses incurred	<u>7,912,656</u>	
Total underwriting deductions		<u>33,591,079</u>
Net underwriting loss		(1,004,873)

Investment Income

Net investment income earned	\$ 4,672,880	
Net realized capital gains	<u>404,853</u>	
Net investment gain		5,077,733

Other Income

Net loss from agents' or premium balances charged off	\$ (3,504)	
Finance and service charges not included in premiums	1,452,900	
Net gain from agents' or premium balances charged off	<u>2,214</u>	
Total other income		<u>1,451,610</u>
Net income before federal income taxes		5,524,470
Federal income taxes incurred		<u>2,661,647</u>
Net income		<u>\$ 2,862,823</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2002		\$27,950,382
Net income	\$ 2,862,823	
Change in net deferred income tax	883,186	
Change in nonadmitted assets	(214,097)	
Surplus adjustments: Paid-in	9,162,750	
Dividends to stockholders	<u>(70,000)</u>	
Change in surplus as regards policyholders for the year		<u>12,624,662</u>
Surplus as regards policyholders, December 31, 2003		<u>\$40,575,044</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 1998 through December 31, 2003

Surplus as regards policyholders, December 31, 1998, per Examination	\$20,269,940
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	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>
Net income	\$ 9,027,063	\$
Net unrealized capital losses		19,401
Change in net deferred income tax	2,465,163	
Change in nonadmitted assets		1,473,233
Cumulative effect of changes in accounting principles	1,461,762	
Surplus adjustments: Paid in	13,371,750	
Dividends to stockholders	<u> </u>	<u>4,528,000</u>
Totals	<u>\$26,325,738</u>	<u>\$6,020,634</u>

Net increase in surplus as regards policyholders	<u>20,305,104</u>
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Surplus as regards policyholders, December 31, 2003, per Examination	<u>\$40,575,044</u>
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COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Uncollected Premiums and Agents' Balances in the Course of Collection Deferred Premiums, Agent's Balances and Installments Booked but Deferred and Not Yet Due

The Company's method of accounting for advance premiums is not in compliance with SSAP No. 53, paragraph 13, which requires advance premiums to be recognized as a liability. It records advance premiums as a credit to accounts receivable. It is recommended that the Company comply with SSAP No. 53, paragraph 13. The amount is immaterial, and no adjustment was made.

(2) Losses and Loss Adjustment Expenses

A Casualty Actuary with the California Department of Insurance (CDI) reviewed the analysis of loss and loss adjustment expense reserves prepared by the Company's independent actuary and concurred with the conclusion that the reserves were reasonable.

(3) Taxes, Licenses and Fees

California Insurance Code (CIC) Section 1872.8(a) states, in part, that each insurer doing business in the State of California must pay an annual Vehicle Fraud Assessment Fee for each vehicle insured under an insurance policy it issues in California. The fee provides funding for the increased investigation and prosecution of fraudulent automobile insurance claims and automobile theft in the State of California.

During the course of this examination, it was noted that the Company failed to remit the Vehicle Fraud Assessment Fee for the second quarter of 2001 as required by the CIC. The Company subsequently remitted the amount due to the CDI in compliance with the CIC.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Corporate Records (Page 6): It is recommended that the Company establish written procedures to require annual conflict of interest reporting for its directors, officers and key employees.

Reinsurance (Page 8): It is recommended that the reinsurance agreements be amended to meet the requirements of California Insurance Code (CIC) Section 922.2(a)(2) and remove any reference to New York laws from the insolvency clause.

It is recommended that the reinsurance agreements be amended to remove any reference to “insolvency.”

It is recommended that the reinsurance agreements be amended to comply with SSAP No. 62, paragraph 7, of the NAIC Accounting Practices and Procedures Manual.

It is recommended that the governing law clause in the environmental liability quota share reinsurance agreement be deleted.

Comments on Financial Statement Items - Uncollected Premiums and Agents' Balances Booked but Deferred and Not Yet Due (Page 16): The Company's method of accounting for advance premiums is not in compliance with SSAP No. 53, paragraph 13, which requires advance premiums to be recognized as a liability. It is recommended that the Company comply with SSAP No. 53, paragraph 13.

Prior Report of Examination

Management and Control – Conflict of Interest (Page 4): The Company has not established written procedures to require annual conflict of interest reporting for its directors, officers, and

key employees. During the current examination period, the Company did not fully comply with the recommendations made.

Corporate Records (Page 6): It was recommended that the Company comply with CIC Sections 1200 and 1201 on a regular basis. The Company is now in compliance.

Accounts and Records (Page 8): It was recommended that the Company ensure that it will be able to access the underlying data in the new claim system. It was also recommended the Company develop controls to verify the underlying data and be able to supply detailed information when requested. The Company is now in compliance.

Accounts and Records – Information System Control (Page 8): Weaknesses noted in the Company's general controls over its information systems were presented to the Company along with recommendations to strengthen its controls. Some of these same recommendations were also incorporated in the summary of the current information systems review provided to the Company.

Comments on Financial Statement Items - Cash and Short-Term Investments (Page 13): It was recommended the Company adopt a formal procedure with respect to unpaid cash items and to the reporting of such items, in accordance with the unclaimed property laws of the applicable states. The Company is now in compliance.

Comments On Financial Statement Items – Premiums and Agents' Balances in Course of Collection and Premium and Agents' Balances and Installments Booked and Deferred and Not Yet Due (Page 13): It was recommended that all installment premiums due from a specific policyholder be nonadmitted if one premium amount due from that policyholder is more than three months past due; and that the Company apply credit balances over three months past due to debit balances for the same policyholder. The Company is now in compliance.

Comments on Financial Statement Items - Electronic Data Processing Equipment (Page 14): It was recommended the Company establish procedures so as to be in compliance with CIC Section 1194.95. The Company is now in compliance.

ACKNOWLEDGEMENT

Acknowledgment is made of the cooperation and assistance extended by the Company's officers and employees during the course of this examination.

Respectfully submitted,

/S/ _____
Kyo Chu, CFE
Examiner-In-Charge
Associate Insurance Examiner
Department of Insurance
State of California